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Supreme Court of the United States

OCTOBER TERM, 1940

No. 465

IN THE MATTER

of

DEEP ROCK OIL CORPORATION, a corporation,
Debtor,

STANDARD GAS AND ELECTRIC COMPANY,
Petitioner,

against

JOHN M. TAYLOR, *et al.*, as the Preferred Stockholders Independent Committee, JOHN J. SHINNERS, *et al.*, as a Reorganization Committee of Deep Rock Oil Corporation, H. N. GREIS, Trustee of Deep Rock Oil Corporation, THE SECURITIES AND EXCHANGE COMMISSION, Intervenor, and DEEP ROCK OIL CORPORATION.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT AND BRIEF IN SUPPORT THEREOF

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a corporation,
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JOHN M. TAYLOR, *et al.*, as the Preferred Stockholders Independent Committee, JOHN J. SHINNERS, *et al.*, as a Reorganization Committee of Deep Rock Oil Corporation, H. N. GREIS, Trustee of Deep Rock Oil Corporation, THE SECURITIES AND EXCHANGE COMMISSION, Intervenor, and DEEP ROCK OIL CORPORATION.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

To the Honorable, The Chief Justice and the Associate Justices of the Supreme Court of the United States:

Your petitioner, STANDARD GAS AND ELECTRIC COMPANY, by its counsel, A. Louis Flynn, Jacob K. Javits and Wilbur J. Holleman, alleges:

A. STATEMENT OF THE MATTER INVOLVED*

Order appealed from.

The instant petition seeks to review an order in the reorganization proceedings of Deep Rock Oil Corporation, a Delaware corporation (hereinafter referred to as "Deep Rock" or "Debtor"). By this order (R. 159, f. 219), the District Court for the Northern District of Oklahoma (1) denied to Standard Gas and Electric Company (hereinafter referred to as "Standard") any participation in the reorganization of Deep Rock or against the estate of Deep Rock, "although", the District Judge decreed, "from the evidence it might be found that Standard has a valid claim" (R. 160); (2) adjudicated that the Debtor is the owner of all the issued capital stock of Deep Rock Oil and Refining Company (hereinafter referred to as the Refining Company), and of the Bradstreet Properties and of the Cracking Plant; (3) directed Standard to deliver to the Trustee of the Debtor a note of the Refining Company for the principal sum of $1,894,592.11, "marked paid", a deed to the Cracking Plant and certificates for the issued and outstanding stock of the Refining Company; and (4) adjudicated as invalid the claim of Standard against the Refining Company upon the note of $1,894,592.11 and for $8,227.94 in cash loaned by Standard to the Refining Company since the inception of the receivership proceedings and

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*This case is the result of further proceedings which followed the decision of this Court in *Taylor* v. *Standard Gas and Electric Company*, 306 U. S. 307, 59 S. Ct. 543, 83 L. Ed. 669 (1939). Subsequent to that decision, Standard filed an amended proof of debt. This petition relates to proceedings affecting the amended proof of debt (R. 91).

for $41,706.25 loaned by Standard to the Refining Company prior to the inception of the receivership proceedings.

From this order, Standard appealed to the United States Circuit Court of Appeals for the Tenth Circuit. Motions were made to dismiss the appeal and, in one case, to either dismiss the appeal or affirm the order below (R. 1362, *seq.*). The Circuit Court of Appeals denied the motions to dismiss the appeal (113 F. (2d) 266, 267; R. 1378, 2078) and without receiving briefs or hearing arguments on the merits, affirmed on the merits the order of the District Court. Circuit Judge Huxman wrote an opinion of affirmance in which Circuit Judges Phillips and Bratton concurred (113 F. (2d) 266, R. 1372, f. 2071).

Proceedings subsequent to the decision by this Court of *Taylor* v. *Standard*, 306 U. S. 307.

This appeal results from further proceedings had in the reorganization proceedings of Deep Rock consequent upon the decision of this Court in *Taylor* v. *Standard Gas and Electric Company, et al.*, 306 U. S. 307 (hereinafter referred to as the *Taylor* case). After the decision of the *Taylor* case by this Court on February 27, 1939, the parties to the cause sought to agree upon a new plan of reorganization susceptible of confirmation by the District Court pursuant to the mandate of this Court in the *Taylor* case (R. 44). These negotiations culminated in an agreement upon principles of a plan of reorganization on May 5, 1939 (R. 45, 1327, *seq.*), which the District Court directed be submitted to counsel for the Trustee for a report. The report of counsel for the Trustee suggested certain minor modifi-

cations in the agreed upon principles and advised the Court that:

> "We know of no other way by which effect can be given to the opinion of the Supreme Court, which recognizes Standard Gas and Electric Company as being entitled to a common stock interest in the reorganized company, despite the fact that the claims of creditors and rights of preferred stockholders, to which Standard is subordinated, exceed the appraised value of the debtor's assets as approved by the Supreme Court. Except through this stock there is no way for Standard to participate in ownership of the new company and at the same time be in the subordinate position required by the Supreme Court"* (R. 1325).

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*The plan agreed upon provided for $11,000,000 of Fifteen Year Debentures (to go to note holders), and 250,000 shares of Class A common stock of the par value of $10 each, having cumulative preferred dividends at the rate of $1.50 a share per annum and in liquidation a preferential right to $25 per share plus accumulated dividends. All the shares of Class A stock were to have voting rights. 200,000 shares of Class A stock were to go to the present preferred stockholders, the remaining 50,000 shares to be available for payment in kind of such compensation as the District Judge might allow to counsel for the Independent Preferred Stockholders Committee. In addition, there were to be issued 400,000 shares of Class B common stock, each share of which was to be entitled to one vote; the Class B common stock was to be junior in right to dividends and in liquidation to the Class A stock, and was to be subject to the further restriction that no dividends be paid on the Class B common stock unless an amount equal to such dividends be paid into a sinking fund for retirement of Class A stock until one-half of the Class A stock had been retired. Of the Class B common stock, 25% (100,000 shares) was to go to the note holders; 12½% (50,000 shares) was to go to the holders of the preferred stock; and the remaining 67½% (250,000 shares) was to go to Standard. Until the new debentures

On June 14, 1939, an appearance in the proceeding was entered in the District Court on behalf of the Securities and Exchange Commission (hereinafter referred to as the S. E. C.). The S. E. C. immediately indicated to the representatives of security holders that it considered that Standard was entitled to no participation in the reorganization (R. 45, 46). Thereupon the Reorganization Committee declined to file a plan based on the principles which had been agreed upon in writing by its representatives and those of the various parties; further efforts of the parties to agree upon a plan of reorganization conforming to the mandate and opinion of the Supreme Court granting participation to Standard were fruitless. It is obvious, therefore, that the parties recognized a right in Standard to participate in the reorganization based on the Supreme Court's decision but that it was the position of the S. E. C. in endeavoring to promote in this case a general policy not designed for or applicable to this case which made it impossible for the parties to consummate their agreement and close the case (R. 46, 47).

"Speculators'" Purchases of Deep Rock Securities

On December 15, 1939, the District Court, on its own motion, entered an order directing that the holders of notes

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had been paid in full, the voting rights of all the stock were to be exercised by five voting trustees, one of whom was to be designated by the Reorganization Committee, one by the Independent Preferred Stockholders Committee, one by Standard and two by the District Court. It will be observed that the voting shares allocated to Standard (250,000 shares) did not exceed the voting rights allocated to the preferred stockholders and were substantially less than the aggregate voting rights of the note holders and preferred stockholders (R. 1327, *seq.*).

and preferred stock of the Debtor file statements with the Trustee stating the date of purchase or acquisition of their securities and the prices paid therefor (R. 72, f. 93). On January 29, 1940, the Trustee filed a report under said order (R. 123, ff. 174 *seq.*) to which report was attached a summary of the statements received from the holders of notes and preferred stock in response to such order of the District Court (R. 133). Of the holders of 70.13% of notes who responded to the order of the District Judge, approximately two-thirds had purchased their securities subsequent to March 1, 1933 (the date of the beginning of the proceedings), some at prices as low as 20% of the principal amount of such notes (R. 133). The precise prices paid by note holders were not disclosed, but attached to the report of the Trustee are statements of the market prices at which notes and preferred stock of the Debtor were traded in since March 1933 (R. 134-137). It will be observed that since March 1933, such notes have been traded in "flat" *i.e.,* the prices have been without regard to accrued interest. It will also be observed that out of the $4,114,500 principal amount of notes reported to have been acquired after the inception of the proceedings, $3,000,000 principal amount were acquired at less than 75% of face value, "flat" (*i.e.,* without regard to accrued interest) (R. 133). Accrued interest during the receivership—not paid for by those who purchased their securities "flat"—amounts to $4,200,000 or 42% of principal, according to the order of which petitioner complains.

The report shows with respect to the preferred stock that reports were received from the holders of 62.75% of the outstanding stock; that approximately 25% of the reporting stock was purchased or acquired subsequent to

March 1, 1933, some at prices less than $5 per share and all but 512 of such reporting shares at less than $25 a share (R. 134). Accrued dividends on the preferred stock since March 1933—not earned—amounts to $3,150,000!

It is a fair and reasonable inference that the greater number, if not all, of the holders of the 29.87% of outstanding notes and of the holders of the 37.25% of outstanding preferred stock who failed to report their transactions since March 1, 1933 purchased at or near the bottom of the prices reported during such period, *i.e.*, notes at 20% to 25% of the principal amount thereof "flat", and preferred stock at about $5 a share. (Compare Trustee's statement of the market prices for Deep Rock's notes and preferred stock during the receivership period, beginning March 1, 1933 (R. 134-137).) The District Judge, in his findings of fact, found that "since the inception of the receivership proceedings and the reorganization proceedings of the Debtor", large percentages of notes and preferred stock of the Debtor have been acquired by the present holders "at prices substantially below the principal amount thereof in the case of notes, or the preferential rights in liquidation in the case of the preferred stock" (R. 150).

Standard's Amended Proof of Debt, Filed December 28, 1939

On December 26, 1939, the District Court, by an order duly entered (R. 88), as amended by order of December 28, 1939 (R. 90), authorized the filing by Standard of an amended proof of debt. On December 28, 1939, Standard filed its amended proof of debt (R. 91, *seq.*).

The petition for leave to file the amended proof of debt (R. 74, *seq.*, f. 97, *seq.*) asserted that no disposition on the merits had ever been made of the original claim filed by Standard, that Standard is a publicly owned corporation with 37,068 stockholders representing a capital and surplus of $110,000,000 subject to indebtedness of $71,209,500 to 21,467 debenture holders and noteholders, that Standard (which was itself reorganized under Section 77B of the Bankruptcy Act in 1935-1938) is managed by a Board of Directors of whom a majority are elected by the public security holders of Standard, for whose benefit and on whose behalf Standard's claim is asserted, that in the absence of an agreement on a plan of reorganization it was necessary for the court to determine the amount of the claim of Standard, that the District Court on its own motion had directed the holders of notes and preferred stock to file with the Trustee a subscribed statement in writing showing, among other things, the date of purchase of notes and preferred stock of the Debtor and the prices paid therefor, that since the inception of the receivership proceedings notes of the Debtor had been purchased at prices as low as 20% of the principal amount thereof and preferred stock of the Debtor had been purchased at prices as low as $1 a share (inclusive of any dividend accumulations), that the holders of notes and preferred stock of the Debtor who acquired such interests during the pendency of the reorganization proceedings sought to be unjustly enriched in the proceedings at the cost and expense of the innocent security holders of Standard, that the court should take into consideration the prices paid by the present holders of notes and preferred stock of the Debtor in determining the propriety and extent of any subordination of any part

of the claim of Standard, that the proposed amended proof of debt would simplify the issues and eliminate from the claim all matters not relevant to a final determination of the claim on its merits. The petition requested the court to take testimony on the amended proof of debt with respect to the merits thereof and with respect to any equities pertaining thereto. The order granting leave to file the amended proof of debt was not appealed from.

The amended proof of debt (R. 91 *seq.*, f. 121 *seq.*) is for a claim in the amount of $6,129,248.36, and, unlike the original proof of debt (which is based on a running open account from 1919 to 1933), is based exclusively on specific transactions between Standard and Deep Rock occurring between February 24, 1928 and February 28, 1933. Briefly, the amended proof of debt includes only items (accruing within the period specified) of cash advanced by Standard to or for the benefit of Deep Rock (primarily to or for payment to strangers), less cash repaid by Deep Rock to Standard, interest, dividends declared but not paid on preferred and common stock of the Debtor owned by Standard, interest on Deep Rock securities owned by Standard, and charges assigned to Standard by the Management Corporation for engineering and management services.

A summary of the items included in the amended proof of debt is printed at page 100 of the Record. It is followed by detailed schedules supporting every item of claim (R. 101-108).

Proof Offered in Support of Standard's Claim

On January 29 and January 30, 1940, the District Court for the first time in this case heard testimony with respect to the merits of the amended claim of Standard Gas and

Electric Company* (R. 1185-1313). At the same hearing, and, therefore, mingled in the record of such hearing, the District Court also considered a proposed amended plan of reorganization filed by the Reorganization Committee (after intervention by the S. E. C. and following its views), and heard evidence with reference to the value of the assets of the Debtor, submitted in connection with such plan.

At the hearing on its claim, Standard introduced evidence, substantially uncontroverted, fully supporting every item in its amended claim (R. 1264, *seq.*). Vouchers and checks were produced in proof of every cash disbursement comprehended in Standard's claim (R. 1266). Standard also introduced uncontroverted evidence, in the form of the report of the Trustee (R. 123, *seq.*; 1239), with respect to the prices at which notes and preferred stock of Deep Rock have been acquired by their holders during the receivership period; the fact that Standard is in effect a corporate description for 37,068 holders of the stock and 21,467 holders of the notes and debentures of Standard (R. 1268); the fact that the cost to Standard of money during the period covered by the amended proof of debt exceeded the rate of 7% per annum as charged in the amended claim upon loans from Standard to Deep Rock (R. 1268); the fact that during the period referred to, of the amount comprehended in the proof of debt, $1,000,000 in cash was paid directly by Standard to the note holders of the Debtor

*Previously, the District Court had heard argument only on the question of compromise. Testimony offered before the Special Master with respect to Standard's original claim was introduced in evidence and constitutes a portion of the proof (to the extent relevant) on the amended proof of debt (R. 1262, 1263).

(R. 1269) as interest on their notes and $597,129.75 in cash was paid directly to the public preferred stockholders of the Debtor as dividends on their stock (R. 1269) and $1,300,428.98 in cash was used for operating purposes of the Debtor (R. 1269, 1270).

Mr. Lynch, President of Standard, and personally familiar with the relationships and dealings between it and the Debtor, testified (R. 1296-1307) that in no instance was any loan made by Standard to Deep Rock for the direct or indirect benefit of Standard (R. 1296) nor to obtain "a stranglehold" upon Deep Rock; that Standard had never used its power to compel Deep Rock to borrow money from it (R. 1296); that Deep Rock could not have borrowed money from any source other than Standard except through giving security, something which Standard did not exact (R. 1297); that Standard never interfered in Deep Rock's relationships with its preferred stockholders, creditors or strangers (R. 1297); that Deep Rock's initial capitalization was adequate and that the need for additional capital developed, after Deep Rock started in business, as a result of radical changes in the oil business, a condition not chargeable in any way, directly or indirectly, to factors within Standard's control (R. 1298); that after the refunding operation in 1928, Deep Rock's financial condition was such that it had adequate working capital for all its requirements, and that the need for money, which resulted in the creation of the indebtedness which is the subject of the amended proof of debt, did not arise until 1929, when it came as a result of a decision by the operating officers of Deep Rock to extend its properties (R. 1299); that the dividends paid to preferred stockholders of Deep Rock were paid only because it was in Deep Rock's interest that they should be paid (in order to maintain a satisfactory credit reputa-

tion) (R. 1299, 1300) and not to influence voting rights or for Standard's benefit (R. 1300, 1301); and that Standard was not in the business of selling securities nor interested in maintaining market prices for the preferred stock of Deep Rock (R. 1307).

For the first time since the inception of the proceedings was a record made before the District Judge on the merits of the claim of Standard, and the District Judge asked by Standard to allow its claim on the merits.

Petition of Standard for Equitable Compensation for Its Interests in the Refining Company

On January 29, 1940, Standard had also filed with the District Court a petition relating to the stock of the Refining Company (R. 117, *seq.*). The petition stated in substance that Standard has advanced all the moneys ($2,544,592.11) used in the acquisition of the Bradstreet Properties and Cracking Plant now owned by the Refining Company, all the capital stock of which is owned by Standard; that in 1922 it became necessary for the Debtor to acquire additional oil acreage and a cracking plant, the need for acreage being due to depletion of oil reserves then owned by the Debtor and the need for the cracking plant being due to rapid technological advances in the oil production industry; that the financial condition of the Debtor was such that it lacked the money necessary for the acquisition of such leases and for the erection of a cracking plant; that the Debtor also lacked the credit necessary to enable it to obtain a license for the use of patented processes in the operation of the cracking plant; that the operating officers of the Debtor requested Standard to lend sufficient funds; that between 1922 and October 1, 1925, Standard provided $2,544,592.11, and between October 1, 1925 and

February 28, 1933, $41,706.25 additional, and during the entire period pledged its credit in order to obtain the necessary licenses for the use of patents; that the purpose of the acquisitions was to afford to Deep Rock, the Debtor, the use of the Bradstreet Properties and the Cracking Plant and at the same time to preserve to the fifty-eight thousand security holders of Standard, whose money was being used for the purpose, security for the realization of their investment acquired through the use of their moneys; that legal and/or equitable title to the property so acquired and to the cracking plant has therefore been in Deep Rock Oil and Refining Company since October 1, 1925; that the Debtor has enjoyed all the use, income, issues and profits of such leases of the cracking plant and has paid to the Refining Company for such use in the aggregate only $500,000; that the leases between the Refining Company and the Debtor (described in the opinion of this court in the *Taylor* case) have been objected to on the ground that such leases were not the result of arm's-length bargaining by parties of equal contracting capacity and are and were onerous, inequitable, and an unfair burden on the Debtor; that a great benefit was conferred by petitioner on the Debtor in providing the oil producing premises and cracking plant and making available the licenses for use of patents; that it was essential for Standard to protect its investment disbursed for the acquisition of such oil producing properties and cracking plant from the possible claims of the then bondholders of the Debtor (which bonds have since been satisfied by due payment thereof in cash in full) or otherwise to subject the property so acquired through the disbursements of Standard's funds and the pledge of its credit to the claims of other creditors and stockholders of the

Debtor; that the procedure followed in the acquisition by the Refining Company (the stock of which is owned by Standard) of the Bradstreet Properties and Cracking Plant was undertaken in good faith for the benefit of the Debtor accompanied by an effort made in good faith to protect the advance of new money derived from the fifty-eight thousand public securityholders of Standard; that the receiver and trustee of Deep Rock have successively operated the properties of the Refining Company and during the course of such operation such properties have depreciated in value partly through obsolescence, partly through the removal and extraction of oil, and partly through wear and tear; that the net balance of the moneys paid by Standard for the acquisition of the Bradstreet Properties and the erection of the Cracking Plant and for improvements and additions is $2,073,798.36; that reasonable compensation in the form of interest at 5% per annum, compounded semi-annually on the unpaid balance of these amounts between February 24, 1928 and February 28, 1933 would amount to $649,582.97, and from February 28, 1933 to December 1, 1939 simple interest at the rate of 5% per annum would amount to $919,408.56; that in addition, since the inception of the receivership and reorganization proceedings, petitioner has expended $8,227.94 for corporate purposes of the Refining Company even though control of all the property has been in the trustee of the Debtor; that interest at 5% per annum on Standard's cost is less than the amount of rental reserved in the leases.

Standard requested the court to determine the fair amount of compensation to be paid by the receiver and trustee for their use and occupancy of the premises during the period of administration by the court, and that the

trustee be directed to either pay such amount as determined by the court and surrender possession and control of the Refining Company properties or in the alternative pay to Standard for its interests therein the amount of its investment therein with 5% interest (R. 117-123).

Answers to the petition were interposed by various parties. The answer of the Securities and Exchange Commission (R. 144) contends that the Supreme Court has already considered Standard's interest in the Refining Company property and decided exactly what the District Court decided in the order which petitioner seeks to have reviewed. The Reorganization Committee in its answer takes the same position that the Supreme Court had already adjudicated title to the property, and in addition states that Standard expended only $650,000 for the acquisition of the property; it also states that Standard in 1928 received common stock of the Debtor in cancellation of the open account indebtedness of Deep Rock to Standard, which included rentals of $1,475,000 accrued prior to 1928 (R. 137). The record shows that this stock when received did not materially alter Standard's interest in the Debtor as a common stockholder and was of doubtful value (R. 357, 358). The answer of the trustee (R. 142) says that Standard has spent not more than $500,000 for the acquisition of the properties in question. The answer of the Preferred Stockholders Committee (R. 147) alleges that the Supreme Court had already adjudicated all the issues involved in the proceeding.

The discrepancies between the admission of the trustee that Standard paid $500,000 for the acquisition of the Refining Company properties, and of the Reorganization Committee that Standard paid $650,000 and Standard's assertion that it spent $2,544,592.11 arise in this way:

Standard paid $500,000 in cash initially to the vendor of the Bradstreet Properties (R. 294); an additional $150,000 was paid to the vendor in the form of three notes of the Debtor, which Standard paid at maturity (R. 295); the remaining $1,894,592.11 represents construction costs of the Cracking Plant, the moneys for which were advanced by Standard to Deep Rock for disbursement as construction proceeded (R. 303, 311, 540, 698). These advances were advanced for a special purpose and were made through Deep Rock for convenience during the period of construction; Deep Rock acted as a conduit for these advances (R. 351, f. 535).

The record contains an itemization of every disbursement made by Standard in connection with the acquisition of the Refining Company properties (R. 1332, ff. 1846-1849). The record also shows that Deep Rock profited from the use of the Refining Company's assets to the extent of more than $4,500,000 up to the beginning of the receivership proceedings (R. 312, 467, 891, 892).

At the hearings on January 28 and January 29, 1940, Standard introduced additional evidence in support of its petition (R. 1274, 1275).

No argument was ever had or permitted to Standard on this petition. In the findings of fact and conclusions of law the District Judge nevertheless found that the properties of the Refining Company "were acquired by and for Deep Rock and belonged to Deep Rock" and that "whatever claim, if any, Standard may have arising out of transactions concerning" the Refining Company properties is "that of a creditor having a claim for money against Deep Rock, and said claim is of the identical character of all other claims, if any, of Standard against said Debtor" (R. 150). The order which petitioner seeks to have reviewed

directs Standard to surrender to the Trustee its interest in the Refining Company, including the capital stock and note of that company, and excludes Standard from any compensatory participation in the reorganization of the Debtor.

District Judge Holds Exclusion of Standard from Participation is Inequitable, as Standard Has a Legitimate Claim

At the conclusion of the testimony, the District Court read a memorandum which he had prepared in which he urged a plan of reorganization making provision for Standard's participation (R. 1307 *seq.*) (which plan the District Judge must have considered to be in conformity with the opinion of the Supreme Court). The parties failed to agree upon this plan.

The hearing adjourned and re-convened on February 27, 1940, at which time the District Judge stated at the opening of the proceedings that he had already made up his mind as to the disposition of all matters pending before him, stating (R. 1314, *seq.*):

> "I will tell you what I am going to do about it. I have already made up my mind, and nobody can change it now. *I agree with you it is inequitable to subordinate your claim to the full amount of these note holders, taking into consideration the actual consideration paid by speculators for their notes pending this bankruptcy proceeding,* but the Supreme Court of the United States in this case, without going into details, said your claim must be subordinated to the note holders and to the preferred stockholders.
>
> "Now I will have to get Mr. Martin to get the figures, and I am going to make a finding as to what the record shows as to how much is due on these

notes, that is principal and interest, and how much preferred stock is outstanding, and how much in dividends is due on the preferred stock, and that under the opinion of the Supreme Court of the United States, and I am bound by it, you are subordinated to those claims, and therefore your claim is valueless, and has no value, and that you cannot have any part or participation in the reorganization of this company. Now that is the order I enter in the case.

"Mr. Levitan: I respectfully except to that, Your Honor, because I don't think the Supreme Court requires that subordination.

"The Court: You can take it back up there. * * *

"The Court: No. I will say this. I will say, yes, if there was any value above the note issue and the preferred stock, whatever this amended claim shows, *they would have a legitimate claim*" (R. 1316).

The district court refused to hear any argument with respect to the Refining Company petition, stating:

> "The Court: You understand what I want. I am trying to fix it so you will get your appeal" (R. 1317).

The Extent of the Subordination Decreed by the District Court.

On February 29, 1940, the District Court entered the order (R. 159, f. 219), which results in this petition, decreeing that the claims of creditors and note holders must be satisfied in full before Standard is entitled to participate in the assets of the Debtor, in liquidation, reorganization, or in any other manner whatsoever, the words "in full"

being defined for the notes as $10,000,000 principal amount plus interest at 6% per annum from March 1, 1933, amounting to $4,200,000, and for the no par value preferred stock as $5,000,000 plus dividends at the rate of $7 per share per annum on 50,000 shares, since January 1, 1931, amounting to $3,150,000 (thus disregarding completely the facts about the acquisition of notes and preferred stock by "speculators" during the pendency of the proceedings), and decreeing that the claim of Standard as a creditor and its interest as a common stockholder of the Debtor "are without value, since the claims of the creditors and note holders and the interests of the preferred stockholders substantially exceed the value of the assets of the Debtor", that Standard is not entitled to participate in the reorganization of the Debtor, that the amount for which the claims of Standard should be allowed is unimportant and immaterial and it is unnecessary for the court to pass upon the amount or validity of the claim of Standard although, the District Judge found, "from the evidence it might be found that Standard has a valid claim" (R. 160), that the Debtor owns all the stock of the Refining Company and is the owner of the Bradstreet Properties and of the Cracking Plant and that Standard should transfer to the Trustee the note of the Refining Company held by it, in the amount of $1,894,592.11, "marked paid", and deeds of conveyance of the Cracking Plant and certificates covering all the issued stock of the Refining Company, that Standard has no valid claim on account of the $1,894,592.11 note of the Refining Company held by it, or for $8,227.94 (being the amount of cash expended by Standard for the corporate purposes of the Refining Company since the beginning of the receivership, March 1, 1933) or for the amount of $41,706.25

loaned by Standard to the Refining Company for the maintenance and operation of the Bradstreet Properties and Cracking Plant.

Findings of Fact by the District Court

The findings of fact by the District Court (R. 148) substantially parallel the order appealed from. No findings were made as to the amount of Standard's claim—although Standard requested such findings (R. 153, *seq.*)—and although the District Judge stated in the order that "from the evidence it might be found that Standard has a valid claim" (R. 160). No controversy has ever existed about the fact that Standard has a valid legal claim for most of the items comprehended in its amended proof of debt.

The Opinion of the Circuit Court of Appeals

The opinion of Judge Huxman (R. 1372) recites briefly the history of the cause, the order appealed from, the contentions of Standard that this court had not decided in the *Taylor* case that Standard must be excluded if the assets of the Debtor were less than the sum of (1) principal and interest accrued on the notes during the receivership, and (2) liquidation priorities of preferred stock over the common stock, including dividends accrued during the receivership proceeding.

Standard's additional contentions before the Circuit Court were that in the *Taylor* case, this court, in the exercise of powers conferred by subsection (b) (2) of Section 77B of the Bankruptcy Act (which relates to what a plan of reorganization may include), had ruled that the plan of reorganization and concomitant order of compromise must be reversed since "equity requires the award to preferred

stockholders of a superior position in the reorganized company," 306 U. S. 307, 323; that in the *Taylor* case, this Court had disapproved the offer of compromise because the plan of reorganization "subordinated preferred stockholders to Standard"; that this Court had held in the *Taylor* case that if a reorganization is effected control should be divided so that preferred stockholders have at least equal voting rights with Standard and a right of participation in the equity prior to that of Standard, 306 U. S. 307, 324; that this Court had not adjudicated the merits of Standard's claim and had not decided that Standard must or may be excluded; that in its opinion in the *Taylor* case where it stated "In the present case there remains an equity after satisfaction of the creditors in which only the preferred stockholders and Standard can have an interest," (306 U. S. 307, 322) this Court had left open the precise formula for a division of the equity remaining after satisfaction of the debt (notes), and indicated that such division should be according to equitable principles; and that this Court had not sanctioned expressly or inferentially the palpable inequity of the decision of the District Court.

In answer to these contentions, which the opinion does not consider, Judge Huxman merely held that this Court had decided that Standard's claim had been subordinated to the position of the preferred stockholders of Deep Rock for all purposes. The Circuit Court made no attempt to consider the equities of Standard's position *vis-a-vis* the equities of the positions of preferred stockholders and note holders of Deep Rock. The Circuit Court assumed that Standard has a valid claim and then erroneously assumed, without analysis or discussion, that the mandate of this Court in the *Taylor* case required "that the claim of note

holders be first satisfied; that the claim of the preferred stockholders be next satisfied; and that any balance remaining belonged to Standard" (113 F. (2d) 266, 269; R. 1377). The only explanation which the Circuit Court had for those paragraphs of the opinion of this Court in the *Taylor* case, which give a right of participation to Standard, was that if before the final consummation of any plan of reorganization the assets of Deep Rock should so increase in value that there would be a substantial equity over the notes plus all accrued interest and the preferred stock plus all accrued dividends, whether earned or not, to be applied to the satisfaction of Standard's claim, the court could make this equity available to Standard! (113 F. (2d) 266, 269; R. 1376, 1377)

The Circuit Court made no mention at all in its opinion of Standard's contentions with respect to the Refining Company, as set forth in the petition of January 29, 1940 (R. 117; see pp. 12-16, *supra*).

The decree of the Circuit Court of Appeals was entered on June 29, 1940. From the decision of the Circuit Court of Appeals, this petition for certiorari is taken.

B. THE QUESTIONS PRESENTED

1. Did the Supreme Court in *Taylor* v. *Standard Gas and Electric Co.*, 306 U. S. 307, decide (as assumed by the District Court and by the Circuit Court of Appeals) that the note holders of Deep Rock must first be satisfied to the extent of the full principal amount of their notes ($10,000,000) plus interest throughout the receivership and reorganization proceedings ($4,200,000, *i.e.*, at the rate of 6% per annum), and that the holders of the no par value

preferred stock must be next satisfied to the extent of the preference in liquidation of the preferred stock over common stock, including accrued dividends throughout the receivership and reorganization proceedings (even though unearned) (a total of $8,150,000 of which $3,150,000 represents accrual of dividends at the rate of $7 per share per annum), before any provision may be made for Standard as a creditor, regardless of the fact that since the beginning of the receivership and reorganization proceedings, "speculators" have acquired notes at prices as low as 20% of the principal amount thereof "flat" (*i.e.* inclusive of interest) and preferred stock at prices as low as—and, indeed, less than—$5 per share?

2. Does equity permit the preclusion of Standard from participation in the reorganization of Deep Rock, solely for the benefit of holders of notes and preferred stock of Deep Rock, a substantial part of which securities were acquired at small fractions of face amount during the receivership and reorganization proceedings of Deep Rock, in view of the uncontroverted fact that cash advanced by Standard to Deep Rock within the period covered by the amended proof of debt, in excess of repayments, amounted to $3,082,689.91 (R. 1267), of which $1,000,000 was paid directly to the holders of notes on account of interest on their notes, and $597,129.75 to the holders of preferred stock on account of dividends, and $1,300,428.98 was provided for the Debtor for the purpose of enabling it to pay essential operating and corporate expenses?

3. Whether the principles of a court of equity do not require that Standard as a creditor for $6,129,248.36 (or such lesser amount as the court might determine in an adjudication on its own equities of each item of claim) be

accorded fair participation in the reorganization of the Debtor?

4. Did the Supreme Court decide in the *Taylor* case that Standard must be deprived of its stock in the Refining Company and of the note of the Refining Company, representing a net cash investment therein of $2,082,026.30, without receiving compensation therefor notwithstanding the fact that the Debtor enjoyed vast financial benefits through the use of the properties of the Refining Company?

5. Were the standards of due process of law and the standards of equity, as established by this court, violated by the District Court in directing Standard to transfer to the Trustee without compensation the stock and note of the Refining Company and the Bradstreet Properties and Cracking Plant?

6. Did the District Court have jurisdiction to adjudicate the validity of the claim of Standard against Deep Rock Oil and Refining Company and to order cancellation of that claim?

C. REASONS FOR GRANTING CERTIORARI

The reasons for granting certiorari in this case are:

1. Correction of grave injustice.

A grave injustice and inequity has been done to fifty-eight thousand public security holders of Standard (R. 1268) whose interests have been entirely excluded from participating in the reorganization of Deep Rock by a decision which the District Judge who rendered it considered inequitable (R. 1314). The District Judge acted in

the belief that he was under compulsion of the decision of this Court in the *Taylor* case to render such decision (R. 152); as a matter of fact no such compulsion existed, since the *Taylor* case did not decide the issues involved in the order complained of; the *Taylor* case dealt with a voluntary, agreed-upon reorganization, whereas the order now appealed from is one of complete bar and foreclosure against Standard.

Standard has a net cash investment in Deep Rock of $20,567,763.74 (R. 1270). The claim of Standard includes $3,000,000 of net cash advanced by Standard since 1928 (*i. e.,* in excess of cash repayments); of these net cash advances, the sum of $1,000,000 was paid directly to the note holders of the Debtor, the sum of $597,129.75 was paid directly to the public preferred stockholders of the Debtor, and the sum of $1,300,428.98 was provided to the Debtor for operating purposes (R. 1269, 1270). In addition, the Debtor, and through it the holders of notes and preferred stock, have enjoyed vast financial benefits from the exploitation of the Refining Company properties, paid for by Standard (R. 307, 313, 891, 892, 1333-1335). The order below gives this property to the holders of notes and preferred stock outright, without providing any compensation to Standard. Note holders have enjoyed the direct benefit of the payment to them of $1,000,000 of Standard's money, and preferred stockholders have enjoyed the direct benefit of receiving $600,000 of Standard's money. Having received these sums from Standard, should Standard be prevented from recovering them from the Debtor? As to these items there cannot be the remotest suggestion that equity requires a disallowance or subordination. At the least, Standard should stand in no worse position than would have

stood those who received its money, and should not be foreclosed from any recovery. The moneys were advanced solely for Deep Rock's benefit, and not for Standard's benefit (R. 1296, *seq.*).

The palapable inequity of the result of which petitioner complains is the more shocking because of the fact that the note holders and preferred stockholders of Deep Rock now claim a right of priority not only for the principal but also for interest at 6% per annum, and unearned dividends of $7 per share per annum accrued during the entire receivership period while the property was in the custody of and being administered by the court! The unconscionable position of the note holders and preferred stockholders is emphasized by the fact that (as the District Judge found) many of them are "speculators" who acquired their securities during the reorganization proceedings, with full knowledge and notice of the existence of Standard's claim, and seek to make vast profits and be unjustly enriched (R. 150) at the expense of and misfortune to the fifty-eight thousand public security holders of Standard having almost $185,000,000 invested in it (R. 78) and through Standard having over $20,000,000 of cash invested in the Debtor (R. 1270).

Stated pointedly: will this court permit the unjust enrichment of and windfall to "speculators" who purchased their securities at tremendous discounts from face amount on the assumption that Standard had a valid claim, at the expense of Standard's fifty-eight thousand public security holders? What rule of equity or justice could require the shifting of so vast a windfall to one group of persons and the imposition of so grave a misfortune upon another innocent group of security holders?

2. Conflict with applicable decisions of this Court.

This unjust result the courts below have sought to explain on the ground that they were bound by a decision of this Court *requiring* such result. Petitioner submits that such explanation and the decisions based thereon are in conflict with the decision of this Court in the *Taylor* case. The lower courts reached their judgment only through the misreading of this Court's opinion and through the unwarranted extension of this Court's decision.

What this Court decided in the *Taylor* case had to do with the securities which Standard was to receive under a new plan of reorganization—those securities were to be subordinated in character to the securities to be awarded to the preferred stockholders and were to represent voting rights not greater than those allotted to the preferred stockholders. At no place in its opinion in the *Taylor* case did this Court talk of subordination of Standard or Standard's claim except in terms of an award to Standard of participation in a plan of reorganization, or decree that the measure of subordination of Standard's position was principal and interest to date in the case of the notes plus "par" and accrued (though unearned) dividends to date on the preferred stock, or decree that Standard must transfer its interests in the Refining Company to the Trustee without receiving compensation for its investment therein of upwards of $2,000,000 cash.

It is apparent from the opinion of this court in the *Taylor* case that this Court did not attempt to decide the issues which were subsequently drawn; it is clear too that this Court's opinion assumed that the parties would ultimately agree on a new plan of reorganization, consistent with the

opinion. This Court directed the lower Court to apply to any further proceedings the precepts of equity. Because of the opposition of the Securities and Exchange Commission to any participation by Standard, an agreed-upon plan was ultimately found to be impossible (R. 46). In excluding Standard as a creditor from participating in the reorganization, the District Court and the Circuit Court, apparently without realization that they were doing so, proceeded to extend the decision of this Court in the *Taylor* case to a holding that this Court's opinion *required* that Standard be denied participation, in effect expunging Standard's claim, and refused to consider the merits or the equities. The District Court indicated clearly that equity required a different result (R. 1239, 1314).

Petitioner does not believe that in the *Taylor* case this Court intended to deny Standard participation or that it could have reached such a decision on the basis of the incomplete record then before it, or that this Court would reach so harsh and unjust a result.

To reach the decision below, the District Court and the Circuit Court must have questioned both the arithmetic and the comprehensibility of this Court; for after confirming the $17,000,000 appraisal of the Debtor's assets and deducting the provision made for the note holders, this Court had stated:

> "If a reorganization is effected the amount at which Standard's claim is allowed is not important if it is to be represented by stock in the new company, provided the stock to be awarded it is subordinated to that awarded preferred stockholders. No plan ought to be approved which does not accord the preferred stockholders a right of participation in the equity in the Company's assets prior to that of Standard,

and at least equal voice with Standard in the management" (306 U. S. 307, 324).

Petitioner considers that the quoted portion of this Court's opinion contains a suggestion as to how the standards of fairness might be applied in a subsequent plan of reorganization in this case. These standards were clearly indicated: the securities to be awarded Standard must be subordinate in character to those awarded preferred stockholders, and must enjoy no greater voting right. The District Court and Circuit Court both misunderstood the mandate of this Court. The Circuit Court, seeking to explain away the quoted part of this Court's opinion, offered the strange explanation that what this Court "*could* have contemplated" was that there would be "an enhanced value of these assets" because Deep Rock's property fluctuates greatly and increases rapidly in value! (113 F. (2d) 266, 269; R. 1377).

3. Departure from usual course of judicial proceedings and other conflicts with applicable decisions of this Court.

The District Court so far departed from the accepted and usual course of judicial proceeding (and the Circuit Court of Appeals impliedly sanctioned such a departure) as to call for an exercise of this Court's power of supervision. Petitioner has reference here to the refusal by the District Court to grant petitioner a hearing on its application relative to its interest in Deep Rock Oil and Refining Company. Without considering the issues involved in the petition filed by Standard and without providing for any compensation whatsoever to Standard for its $2,082,026.30 of cash investment, for which it retained a security interest

in the Cracking Plant and Bradstreet Properties,—indeed without a notice that affirmative relief against Standard was being sought or contemplated—the District Court ordered Standard to transfer to the Trustee its interests in the Refining Company. The District Court declined to consider the matter, perhaps with the intention of helping Standard reach this court and a just result, for the District Court stated in this connection "I am trying to fix it so you will get your appeal" (R. 1317). The proceeding of the District Court with respect to the Refining Company denied Standard due process of the law, and the order complained of in its entirety denied Standard the application of the fundamental principle of equity jurisdiction: "he who seeks equity must do equity", *Southern Pacific Company* v. *Bogert,* 250 U. S. 483, 39 S. Ct. 533, 63 L. Ed. 1099 (1919). The Circuit Court of Appeals passed over this situation entirely without comment.

In no pleading before the Court was an issue raised with respect to whether the note of the Refining Company held by Standard was valid or whether Standard should be directed to mark such note "paid", or whether Standard had received payment of such note; in no pleading before the Court was an issue raised as to whether Standard should be affirmatively ordered to transfer the stock of the Refining Company to the Debtor without receiving compensation. Standard was therefore denied notice and hearing, essential prerequisites of due process.

4. An important public issue is involved in this case.

Standard, a publicly owned company with fifty-eight thousand security holders, made very large cash advances

to a subsidiary. In the *Taylor* case, this Court determined that Standard's position as a creditor could not be enforced according to its strict legal priority but only according to the standard of a "court of equity." This standard required that each case be approached on its own facts. The decision which petitioner seeks to have reviewed, however, goes so far as to create grave doubts as to whether any corporation making advances to a subsidiary will not be denied recovery, except in subordination to the claims and interests of all other persons. Thus, a vital question of public law in the administration of publicly owned corporations is involved in the question: Shall the innocent security holders of Standard be deprived of all participation in the Deep Rock reorganization, regardless of the merits of each item of claim (a result which the District Judge considers inequitable), because Standard's relationship to Deep Rock was that of parent-subsidiary and because of acts antedating the reorganization of Standard itself? That is the effect of the decision below, and that decision casts doubt on innumerable corporate balance sheets in this country.

It is submitted that in the interests of justice this court should exercise its power of supervision to correct the grave error which has occurred.

D. RELIEF

Wherefore, petitioner respectfully prays that a Writ of Certiorari be issued out of and under the seal of this Court, directed to the United States Circuit Court of Appeals for the Tenth Circuit, commanding that Court to certify and send to this Court, on a day certain to be therein designated, a full and complete transcript of the

record and of all proceedings in this cause, to the end that this cause may be reviewed and determined by this Court; and that the said decree of the said Circuit Court of Appeals in the said case, and every part thereof, may be reversed by this Court; and that petitioner be granted such other and further relief as may be just and proper.

Dated: New York, September 26, 1940.

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